

Wilburn, Gary Gary.Wilburn@leg.wa.gov

First draft of a carbon cap and trade bill

December 11, 2018 at 12:10 PM

To: Carlyle, Reuven Reuven.Carlyle@leg.wa.gov

Cc: Ormsby,Timm , Cushing,Kimberly , Davis,Chris(GOV)

Senator Carlyle:

Attached per your request is a first draft of a carbon emissions cap and trade bill. There are few "new" ideas in this draft, as it borrows heavily from the Governor's legislation in 2015, along with ideas from Washington's Clean Air Rule, Oregon's draft legislation (which we understand will be updated in the coming days), the BP outline, and a few other sources. For convenience I've included a sectional summary before the bill draft legislation so that it will be entirely in one document.

This draft provides considerably more detail than California's legislation directing and updating their cap and trade program. It is also longer than Oregon's legislation. But it is only a fraction of the length of the California implementing regulations, and we can expect that any rules implementing this legislation will be quite lengthy and detailed. This draft seeks to put some of the details into the legislation, leaving somewhat less to "agency filling in the details" than perhaps was left to CARB with the California legislation.

There are some major policy elements in this draft that will certainly gain the greatest attention. And all of these could be revised to take another direction. These are:

Statewide emission targets. This legislation "aligns" with the updated science, the Paris agreement, and the Ecology 2016 recommendations, to strengthen the 2035 and 2050 goals to eventually reduce statewide emissions to 80% below 1990 levels (it is 50% in current law). Other states have adopted comparable goals, at least for some sectors, and the "deep decarbonization" studies show it is feasible to reach this level. It seems appropriate in this very comprehensive measure to key the declining "cap" toward these levels.

How much of the emissions footprint of the state should be included? Like the Governor's 2015 legislation, this measure would include nearly all sources of emissions above 25,000 tons per year (Chris estimates about 60-65% of statewide missions). The exclusions are also similar to that 2015 legislation as well as the carbon tax proposals in recent years -- marine and aviation fuel (burned outside the state), landfill gas, Transalta, and defense installations. It places the compliance responsibility for fuels at the supplier level, although by agreement that can be shifted to refiners.

EITEs. This draft takes a different approach than the BP outline, which would place in statute a specific and detailed formula for determining who are EITEs, and reduce their compliance to just 10% of what other covered entities must achieve. It is closer to the Oregon approach of a "benchmarking" of energy use intensity, and is probably similar to what California does in making "adjustments" to minimize leakage from EITEs. This draft does contain some industry sectors that must be treated as EITEs, using the list from the initial 2015 Washington cap and trade proposal, although it is far shorter than the carbon tax proposal last session.

Distributing allowances through auctions rather than for free. It appears that nearly all of the California allowances are distributed through auctions (with special "consignment" rules electric and gas utilities). And this appears to be the case with the European Union system and with the Oregon proposal. But it is certainly possible to design a "cap and trade" system in which the caps are set by the state and issued to the covered entities to use for their own compliance, and to buy and sell allowances depending on their needs. Under this approach the "market" would be entirely outside the state with no revenues coming to the state. But it is not likely that Washington could link with California under such a system, as it would likely undermine the allowance prices in their market. Of course this assumes that linkage with California is an important objective of the program.

Linkage with California and other jurisdictions. Linkage appears clearly to be an objective of BP's proposal, and it appears the Oregon legislation includes linkage as an objective. There are strong arguments for linkage by "growing the market" for allowances and thus providing more opportunities for WA covered entities to meet their compliance obligations in less costly ways. But some stakeholders will be wary of linking to California, particularly if their emission reduction targets and thus the carbon market is considerably stronger than Washington's. That might drive up the costs of allowances distributed through linked auctions.

Use of the revenues . Experience has shown that the legislative focus on these comprehensive carbon pricing proposals that drive revenue to the state becomes "how will the money be spent?" And this ends up taking much needed attention away from getting the design of the mechanism right. So this initial draft simply sends the auction revenues to a new account, with very general descriptions of the allowed uses -- promoting cleaner energy, providing a "just transition" to that cleaner energy economy, and mitigating the impacts of climate change.

Preemption. While BP has proposed a very broad preemption of any state or local programs directed at reducing the carbon intensity of energy fuels, this draft has no preemption provisions, and, to the contrary, preserves existing state agency authority. Clearly if the legislation gets traction there will need to be discussion around whether broad "complementary" policies like the Clean Fuels Standard proposal (new term for "LCFS") and the Ecology Clean Air Rule. But there seems to be little strategic value in starting a bill with broad preemption language.

We are now moving into high gear on numerous bills and topics and I wish I had more time to "study up" on the many cap and trade programs already being implemented, such as California's, the Northeast states "RGGI" system for electricity, the EU ETS systems, and maybe even some of the emerging programs in various provinces in China. If I had more time to do this I would probably have stronger convictions on where from a policy standpoint we should land on some of the key policy issues outlined above. But at this point I am very open to making any revisions you feel are needed before sharing with any stakeholders, and we can "learn as we go" on this very complex topic.

Kim Cushing and Chris Davis are copied here because they've also been reviewing the draft. But they have been slammed getting other bills drafted, etc., and I've taken the liberty of getting this draft to you before getting their input, in order to get this in your hands for sharing with various experts and shareholders. Their thoughts about details or the general structure of this draft are welcome.

We are ready to assist in any way you'd like in taking this subject to the next steps. Please let us know how you'd like to proceed.